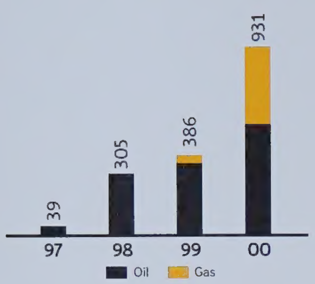
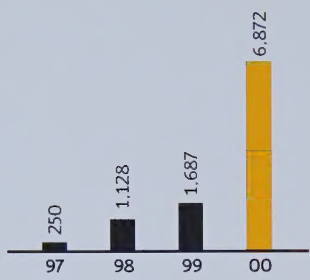
SADDLE RESOURCES INC.

2000 Annual Report

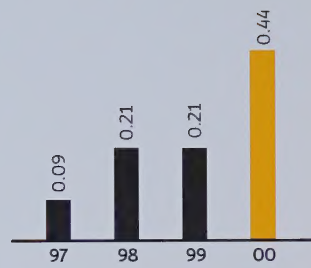
Full Cycle



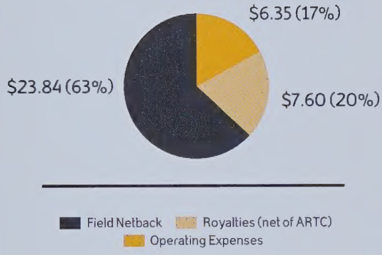
Average Daily Production, (Boe/d @ 6:1)



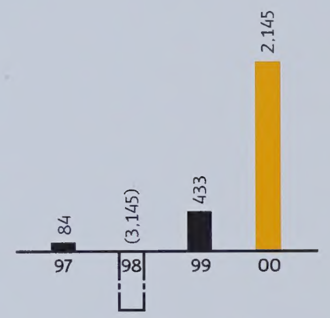
Cash Flow From Operations, ($000)



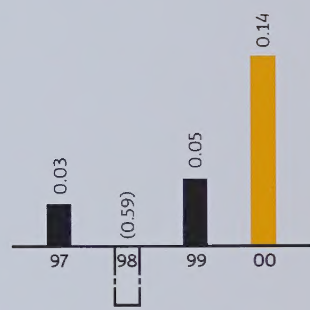
Cash Flow Per Share, ($)



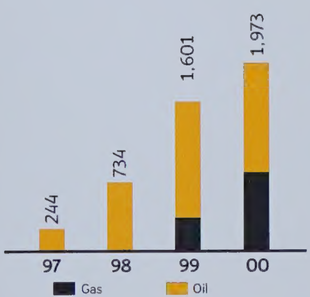
Field Netbacks – 2000
($/Boe @ 6:1)



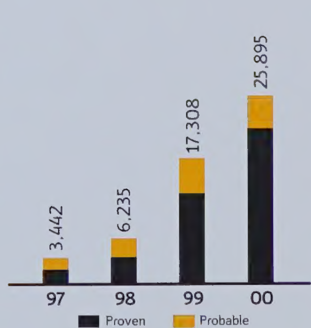
Earnings (Loss), ($000)



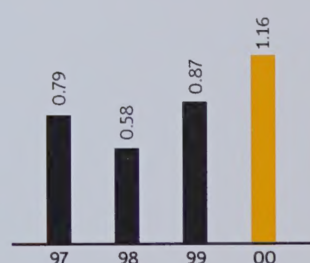
Earnings (Loss) Per Share, ($)



Established Oil and Gas Reserves
(Mboe @ 6:1)



Net Present Value (Before Tax)
15 percent DCF, at Dec. 31 ($000)



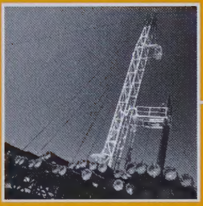
Net Asset Value Per Share
at Dec. 31 ($)

Highlights

(000'S except per share figures)	Year ended Dec. 31, 2000	Year ended Dec. 31, 1999	% Change
FINANCIAL			
Gross revenue	$ 12,869	$ 3,969	224%
Cash flow from operations	$ 6,872	$ 1,687	307%
per share – basic (wt. avg.)	$ 0.44	$ 0.21	110%
per share – diluted (wt. avg.)	$ 0.44	$ 0.16	175%
Field netback ($/Boe 6:1)	$ 23.84	$ 15.64	52%
Earnings	$ 2,145	$ 433	395%
per share – basic (wt. avg.)	$ 0.14	$ 0.05	180%
per share – diluted (wt. avg.)	$ 0.14	$ 0.04	250%
Capital expenditures	$ 11,422	$ 10,017	14%
Working capital surplus (deficiency)	$ (239)	$ (413)	-42%
Long term debt	$ 7,153	$ 2,404	198%
Common shares outstanding			
Weighted average – basic	15,637	8,187	91%
Weighted average – diluted	15,784	10,327	53%
Total outstanding	15,637	8,637	81%
OPERATIONS			
Average daily production			
Crude oil & NGL's (Bbls/d)	544	353	54%
Natural gas (Mcf/d)	2,321	198	1,072%
Oil equivalent (Boe/d @ 6:1)	931	386	141%
Average product prices			
Crude oil & NGL's ($/Bbl)	$ 40.94	$ 28.87	42%
Natural gas ($/Mcf)	$ 5.56	$ 3.13	78%
Wells drilled			
Gross	9.0	1.0	
Net	4.4	0.5	
Success rate (%)	100	0	
Reserves – proved and probable			
Crude oil & NGL's (Mstb)	1,161	1,252	-7%
Natural gas (Mmcf)	4,864	2,090	133%
Oil equivalent (MBoe)	1,972	1,600	23%
NPV @ BT15% ($000) – proved plus 50% probable	$ 23,586	$ 14,689	61%

Saddle Resources Inc.

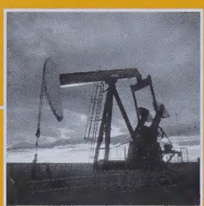
("Saddle") is an emerging energy company engaged in oil and gas exploration and production in Western Canada. The Company's primary area of focus is the Rainbow Lake area of Northern Alberta.



The Company's shares are listed for trading on the Canadian Venture Exchange under the symbol "SRI".

Annual General Meeting – Saddle Resources Inc. invites shareholders to attend the Annual General Meeting on Thursday, June 7, 2001 at 9:30 a.m. at the Metropolitan Centre located at 333, 4th Avenue S.W., Calgary, Alberta.

Full cycle



In its most general sense, the term means "complete measure" or "perfect maturity." It implies knowledge gained through experience. It also implies constant improvement and increased efficiency through the application of this hard won knowledge.

In terms of project investment, Full Cycle describes a project that has evolved to the point that it can fully realize, or reap the rewards of time, effort and capital.

Bill Ward, President

Ken Broadhurst, Senior Vice President

To our shareholders

In the oil and gas industry, Full Cycle begins with the generation of prospects by combining creative thinking with disciplined exploration and mapping techniques. The next stages involve the acquisition of lands on the prospects that have been generated, and further fine tuning the prospects through the application of advanced geophysical and geological technology. The final stage of Full Cycle involves the drilling of wells on the prospects and, if successful, constructing the infrastructure required to produce the reserves in the most economical method possible. Successful operations are then followed up with the exploitation of the prospect by using the knowledge gained through prior efforts in a manner that enables the company to maximize returns on the investment for its shareholders.

Saddle is pleased to advise our shareholders that our principle property at Rainbow Lake is rapidly approaching **Full Cycle**. The year 2000 was a rewarding time for Saddle as we began to realize the benefit of the Full Cycle nature of our efforts. In 1999, we made a firm decision to Build for the Future by embarking on an intensive program to build a **firm foundation of infrastructure and facilities** to capitalize on our extensive prospect inventory. This successfully implemented program set the stage for Saddle's **highly successful drilling program** throughout the 1999/2000 drilling season. Saddle's timing was excellent: the combination of high commodity prices, a successful drilling program and a solid foundation of facilities and infrastructure resulted in a year of record performance in all measurements as outlined for you in this report.

2000 Results and Review

Over the past two years, Saddle has obtained financing, recruited a team, made a major acquisition, generated exploration and development activity, funded an extensive state of the art infrastructure and has increased production to over 930 barrels per day (775 @10:1). This has enabled us to generate record cash flow of $6.9 million in 2000.

We have clearly delivered on our objective to aggressively develop and exploit our asset at Rainbow Lake and have turned the operation into a top notch core property. During 2000, Saddle completed its most successful year of operations to date. Saddle, as operator, drilled a total of nine wells in its core area of Rainbow in Northern Alberta resulting in five (2.4 net) gas wells and four (2.0 net) oil wells for an overall success rate of 100%.

To solidify our production base and optimize cash flows, Saddle invested over 50% of its 2000 capital program in the construction of a major oil facility, gas compression, pipeline infrastructure and the purchase of an operated interest in a second strategically located oil facility. Prior to this, virtually all Company production was processed through third party facilities. At year end 2000, approximately 90% of Saddle's production was processed through Company owned and operated facilities, which resulted in Saddle being able to control its operations and reduce operating costs. Operating costs averaged $7.61/Boe during the year, with this figure incorporating average operating costs of $10.09/Boe in the first

> "OUR PRINCIPLE PROPERTY AT RAINBOW LAKE IS RAPIDLY APPROACHING FULL CYCLE ... WE HAVE CLEARLY DELIVERED ON OUR OBJECTIVE TO AGGRESSIVELY DEVELOP AND EXPLOIT OUR ASSET AT RAINBOW LAKE AND HAVE TURNED THE OPERATION INTO A TOP NOTCH CORE PROPERTY."

half of 2000 (based on a 10:1 ratio). **This improvement in operating costs is a direct result of the implementation of our new facility** which became fully operational in the second half of 2000, along with the addition of key personnel to effectively manage our field operations.

During the year, Saddle made the decision to evaluate a number of strategic alternatives we felt had the potential to maximize shareholder value. At the end of our evaluation, we determined that the interests of the shareholders would be best served by proceeding with the ongoing development of the substantial opportunity base on the Company's existing properties in the Rainbow Lake area. Our share price took an immediate drop on the news that we would not be selling the Company. While our decision not to sell was difficult, we firmly believe it was in the best interest of our shareholders. On a performance basis, 2000 was the most profitable year in the history of Saddle with cash flow soaring to a record $6.9 million ($0.44 per share).

Throughout the strategic evaluation process, Saddle continued to generate drilling prospects at Rainbow Lake. When the decision was made to move forward with a program, Saddle was well positioned to implement a significant work program for the 2000/2001 winter drilling season. Saddle commenced a twelve well drilling program with the successful drilling of a Keg River oil well in December 2000 which currently produces in excess of 150 (75 net) Bbls/d . Saddle also drilled five shallow Bluesky gas wells which were all successful. Saddle has an average 50% working interest in these Bluesky gas wells which will be tied into Saddle's recently expanded gas compression facility and are expected to be on production in May 2001.

A recent seismic program shot by Saddle this winter defined two new shallow Tertiary gas locations which Saddle drilled in March 2001. One of the wells is currently suspended while the other well was highly successful, encountering a 15 metre thick gas column at a depth of 64 metres. The well is expected to initially produce 1.5 to 2.0 (0.75 to 1.0 net) Mmcf per day and appears to have expanded the extent of Saddle's gas reserves in the Tertiary pool. These wells were drilled as a follow up to the two successful Tertiary gas discoveries made last year which continue to produce at a combined rate of 2.0 Mmcf per day. Saddle has demonstrated its expertise in exploring for this non conventional yet prolific gas reservoir which has yielded tremendous value to our shareholders. We have a significant acreage position in this area containing additional Tertiary opportunities which we intend to develop during the next drilling season.

Saddle negotiated a number of creative non-equity financings that enabled us to implement our extensive drilling program. A significant financing component of the 2000/2001 drilling program was secured through a Farmout Agreement (Farmout) which provided for a third party to fund Saddle's $3.4 million share of drilling, completion and equipping costs associated with the drilling of four Keg River oil wells in the Rainbow Lake area. The deal entitled Saddle to retain a carried working interest in each well drilled dependent upon Saddle's initial working

interest and gives Saddle the opportunity to participate in all future development offset wells at its initial working interest. The Farmout provided us with the ability to significantly expand our winter drilling program and maintain a significant working interest in the Farmout wells. We will see immediate cash flow from our cost free carried working interest which will be used to fund further opportunities. During the first quarter of 2001, Saddle drilled four wells pursuant to the Farmout which has resulted in three Keg River oil wells. The Farmout wells are operated by Saddle and will be produced through Saddle's facilities.

Additional financing was obtained through the negotiation of a Joint Exploration Land Fund (Fund) which enables Saddle to spend up to $2.0 million ($1.0 million net) on land and seismic acquisitions. The Fund enables Saddle to invest its capital in drilling and re-completion operations creating immediate increases in cash flow and asset value while at the same time expanding the Company's significant prospect inventory in Rainbow Lake. Saddle is entitled to recover a portion of its ongoing exploration overhead costs and is able to defer repayment until 2002.

Saddle also negotiated arrangements with two separate parties to finance approximately $1.9 million for the construction of additional oil and gas infrastructure at Rainbow Lake. The construction of the new infrastructure will enable Saddle to increase oil and natural gas volumes produced through our 50% owned and operated facilities at Rainbow Lake, including reserves which are currently shut-in. This will have a positive effect on our production and cash flow generated throughout the remainder of 2001 and onward. The financing arrangement provides for Saddle to operate the infrastructure and pay a capital fee to the financiers during the payout of the infrastructure costs, with the option for early payout of the costs to acquire 50% ownership.

Outlook for 2001

Saddle has demonstrated its ability to adapt to difficult market conditions. We have been able to increase shareholder value through creative deal making and the application of our focused technical expertise in a core area. We are clearly moving towards the Full Cycle goals we established for ourselves in 1997.

Fifteen months ago Saddle was predominately an oil producer. **Saddle's production stream now stands at 50% oil and 50% natural gas** through its emphasis on natural gas exploration and development during 2000 and 2001. Saddle is currently conducting an active

exploration program to seek new reserves and production volumes with an emphasis on increasing reserve life index. Saddle has also commenced exploration efforts to develop new core operating areas with the intention of moving them through the Full Cycle process which we believe is critical to realizing full value for our shareholders. We are fully prepared to pursue both natural gas and oil properties as opportunities are identified, including corporate acquisitions.

Saddle has demonstrated its ability to grow and prosper throughout periods of unpredictable activity, commodity prices and financial market cycles and looks forward to continuing to meet these challenges in 2001 and beyond. We would like to thank our directors, management and staff for their significant contribution and support in 2000.

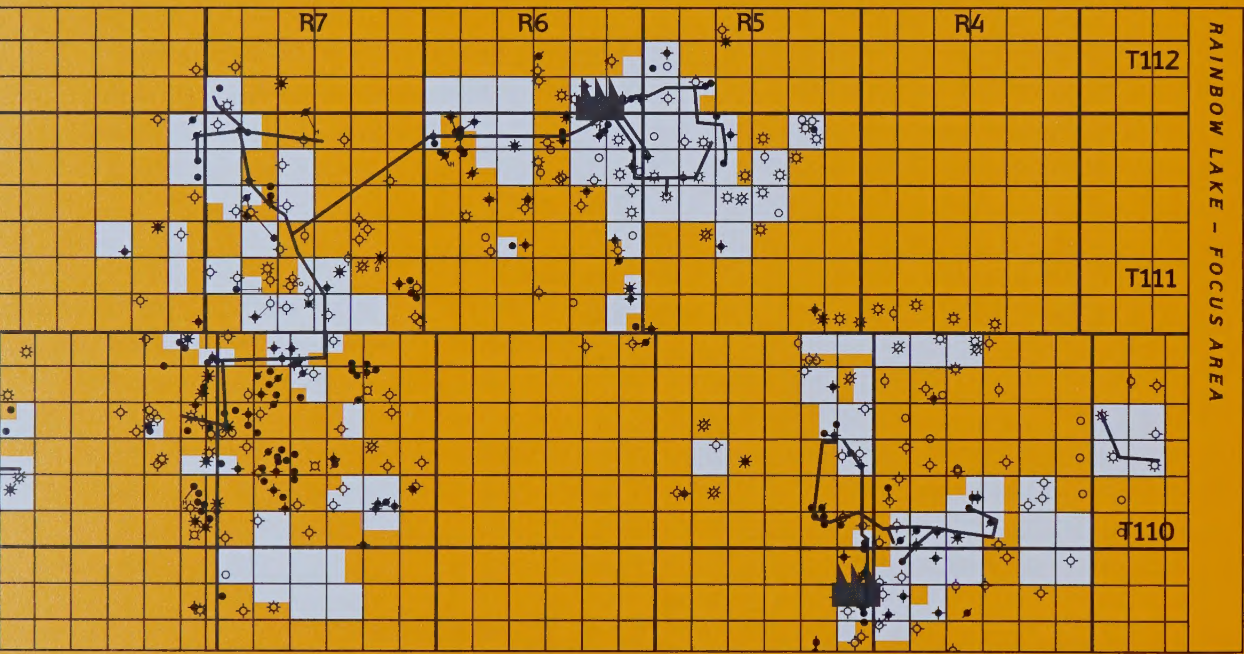
We look forward to updating shareholders at our upcoming Annual Meeting on June 7, 2001,and invite you to call us at any time to discuss the progress of your Company.

On Behalf of the Board of Directors

William S. Ward
President
May 1, 2001

Kenneth L. Broadhurst
Senior Vice President
May 1, 2001

Exploration review



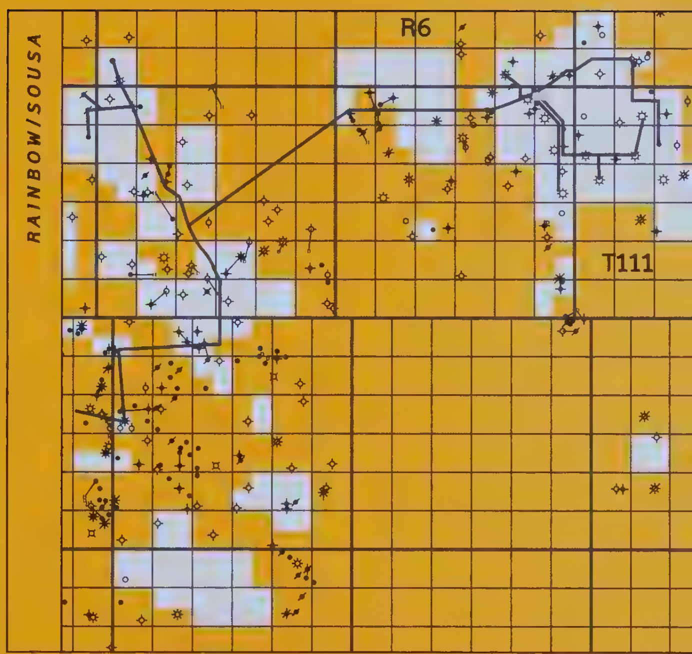
Rainbow lake – focus area

Saddle continued to focus 100% of its efforts in the Rainbow area of Northern Alberta in 2000. During the year, Saddle diversified its production stream to include natural gas as a significant component through a very successful exploration and drilling program. In total Saddle, as operator, drilled nine wells in 2000 resulting in five gas wells and four oil wells for an overall success rate of 100%.

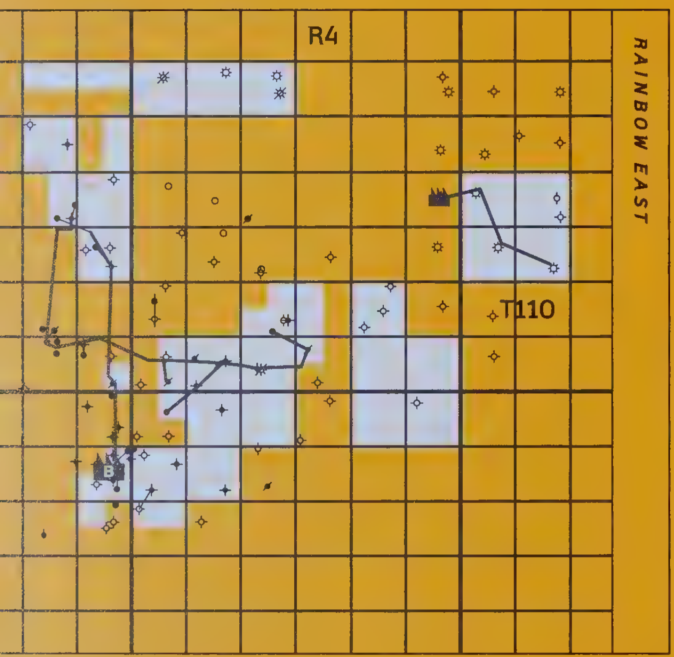
Saddle has established two principle areas of exploration and development in Rainbow, each serviced by Company operated production facilities. The Company refers to these areas as Rainbow/Sousa and Rainbow East.

Rainbow/Sousa

Saddle owns an average 49% interest in 41,885 acres of land in the Rainbow/Sousa area. The lands are tied together by an extensive pipeline and road infrastructure. During 2000, Saddle installed a central oil production and gas compression facility at Rainbow/Sousa. This facility has enabled the Company to develop and expand its oil and gas operations across a four to five township block of land in the area. At December 31, 2000 Saddle had net production of approximately 250 barrels of oil per day (Bbls/d) of light 38 to 40 degree API crude and 1.25 million cubic feet per day (Mmcf/d) of sweet gas from the Rainbow/Sousa area.



During the first quarter of 2000, Saddle drilled three successful gas wells and three successful oil wells in Rainbow/Sousa. The three (1.43 net) successful gas wells drilled by Saddle targeted the Bluesky/Gething formation at a depth of 300 m. The wells were tied into the Company operated gas compressor station located at the 13-36-111-5 W6M facility and commenced production in April 2000 at a rate of 2.5 (1.25 net) Mmcf/d. This shallow gas drilling program was Saddle's first foray into natural gas exploration, and our 100% success rate demonstrates the strength of our exploration techniques. The success of this initial Bluesky drilling program led to the drilling of five (2.55 net) Bluesky gas locations in the first quarter of the Company's 2001 winter drilling program, all of which resulted in successful gas wells to maintain our 100% success rate in this highly profitable gas prospect. Several remaining drilling locations exist on Company lands which will be developed during the 2001/2002 winter drilling season. The three (1.5 net) successful Keg River oil wells drilled by Saddle in 2000 were identified on 3D seismic, with two wells being drilled in the first quarter of 2000, and the third well being drilled in December 2000. At December 31, 2000 Saddle had an inventory of 15 drilling locations on Company lands in the Rainbow/Sousa area, all of which have been identified from Saddle's extensive 3D seismic data base. Saddle drilled two of these locations in the first quarter of 2001 which resulted in one oil well and one dry hole. Saddle's 2001/2002 winter drilling program will include the drilling of several locations in the Rainbow/ Sousa area including the drilling of horizontal wells.

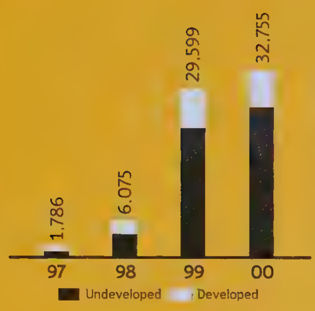


Rainbow East

The Rainbow East area has gained significant importance in Saddle's exploration and development plans as the area has proven to be very prolific for both oil and gas production. Saddle owns an average 45% interest in 17,120 acres of land in the Rainbow East area. At December 31, 2000 the Rainbow East area contributed net production of approximately 250 barrels per day (Bbls/d) of light 48 degree API crude oil and 1.2 million cubic feet per day (Mmcf/d) of sweet gas. The lands in this area are tied together by an extensive pipeline and road infrastructure and are serviced by a Company operated oil processing facility and a non-operated gas compression facility.

During the first quarter of 2000, Saddle drilled one (0.5 net) successful Keg River horizontal oil well which was identified on 3D seismic. The well was placed on production in February 2000 at an initial rate in excess of 400 (200 net) Bopd. Saddle has followed up on this well with the drilling of another successful horizontal well in the first quarter of 2001. One additional drilling location remains offsetting this activity on Company lands.

In the fourth quarter of 2000, Saddle performed one (0.5 net) re-completion operation on a suspended oil well situated in the Keg River LL pool. The operation resulted in production of approximately 75 (38 net) Bopd. Based on the exceptional results obtained from this re-completion, and the interpretation of a six square mile 3D seismic survey shot by Saddle over certain of its land holdings in this area, Saddle commissioned an independent "Reservoir Simulation Study" to determine the remaining recoverable reserve potential in the pool. The study, performed by Kade Technologies Inc. of Calgary, concluded that significant recoverable oil reserves remain on Company lands. Subsequent to the report, Saddle re-completed a second suspended well in January 2001 which resulted in gross production of 25 Bopd. Encouraged by the results of both re-completions, Saddle drilled a step out well to delineate the pool boundaries and to further test the reservoir model developed in the Kade study.



Net Acres, (Acres)

The well was drilled in the first quarter of 2001 and was completed as a successful oil well. Production is slated to commence in early May, 2001.

Early indications from the completion of the well support the Kade model, and further drilling of the pool, including horizontal wells, could begin as early as this summer. Saddle has only booked nominal reserves and value for this property in the January 1, 2001 reserve report, and significant value and reserves could be realized on this property in 2001.

Saddle has also developed a very intriguing shallow gas prospect in the Rainbow East area during 2000. In December 1999, Saddle shot a 2D seismic line across a block of Company lands, and in March 2000, two (1.0 net) successful gas wells were drilled. These wells targeted the Tertiary zone at a depth of 55 to 72 metres. The wells were tied into a non-operated gas compression facility in early May 2000 and produced at a combined initial rate of 3.6 (1.8 net) Mmcf/d. At December 31, 2000 the wells were producing at a combined of 2.4 (1.2 net) Mmcf/d.

Based on this success, Saddle shot a 33 km 2D seismic program in December 2000 that led to the drilling of two additional Tertiary wells in the first quarter of 2001. One well was completed as a successful gas well while the other well was a dry hole. The successful well will be tied into production facilities in May 2001. Saddle has developed a successful exploration strategy for this shallow yet prolific gas prospect which will be used to pursue further opportunities in the area.

Land holdings

Saddle has assembled a strategic and prospect rich land position in the Rainbow Lake area. At December 31, 2000, Saddle's total land holdings were comprised of an interest in approximately 71,805 gross acres and 32,755 net acres.

Saddle's successful drilling program in 2000 evaluated a significant amount of undeveloped acreage. During 2000, Saddle was able to replace and increase its undeveloped acreage with prospect specific land acquisitions at Crown land sales and through property acquisitions which included undeveloped land.

The land inventory now consists of 25,730 net (54,780 gross) undeveloped acres and 7,025 net (17,025 gross) developed acres . Seaton-Jordan & Associates Ltd. independently evaluated the fair market value of the undeveloped lands to be $1.96 million at December 31, 2000.

Saddle recently negotiated a Joint Exploration Land Fund with a third party that will enable Saddle to spend up to $2.0 million on gross land and seismic acquisitions during 2001. The Fund entitles Saddle to recover a portion of its ongoing exploration overhead costs and payment is deferred until 2002. This will allow Saddle to further expand its inventory of undeveloped acreage on high quality prospects that have been identified by Saddle and enable the Company to invest its capital during 2001 on drilling and re-completion operations resulting in immediate increases in cash flow and asset values.

Operations review

Production

All of Saddle's production is situated in the Rainbow area of northwest Alberta. During 2000, the Company averaged production of 544 Bbls/d of oil and natural gas liquids and 2,321 Mcf/d of natural gas production for a combined total of 931 Boe/d (776 Boe/d @ 10:1). This represents a 141% increase over 1999 production of 386 Boe/d (373 Boe/d @ 10:1).

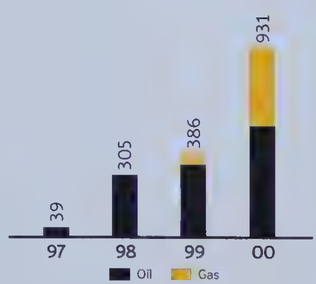
Recognizing the strength of the North American natural gas markets, Saddle initiated a focused push towards a more balanced portfolio of assets on its existing land base. The results of this business plan were reflected in 2000 as natural gas comprised 42% of the Company's production stream up from 9% in 1999. Saddle's natural gas production increased 1,072% in 2000 to average 2,321 Mcf/d up from 198 Mcf/d in 1999.
The successful natural gas exploration program conducted in 2000 has delineated several gas drilling locations and Saddle anticipates further gas production increases for 2001.

During 2000, Saddle's total oil and liquids production increased 54% to 199,019 Bbls from 128,845 Bbls in 1999. On an average daily basis, this equates to 544 Bbls/d in 2000 compared to 353 Bbls/d in 1999. The Rainbow area produces a high quality light crude oil that fetches Edmonton par price less $1.25/Bbl for transportation and quality adjustments. Saddle received an average wellhead price of $40.94/Bbl for its product in 2000 which helped Saddle achieve superior field netbacks of $23.84/Boe ($28.59/Boe @ 10:1).

Facilities

Saddle owns and operates two major oil batteries and one gas compression/dehy station. The 13-36-111-06w6 battery currently handles approximately 5,000 Bbls of fluid per day and 4,000 Mcf/d of gas. The battery has the capacity to process 18,000 Bbls per day and 7,000 Mcf/d of gas. The 9-25-109-5w6m battery currently handles 3,000 Bbl/d of fluid and has the capacity for 4,400 Bbls/d of total fluid.

Saddles has a working interest in 86 miles of pipeline and 63 miles of road infrastructure. In the first quarter of 2000, Saddle had 90% of its production going through third party facilities. With the addition of the 13-36 oil/gas facility, Saddle now has 90% of its production utilizing Saddle operated facilities.
With the achievement of this goal of having complete control of production and infrastructure, Saddle believes shareholders will see an enhancement of value in 2001 and beyond.



Average Daily Production. (Boe/d @ 6:1)

Reserves

Saddle's oil and gas reserves were evaluated by Sproule Associates Limited as at January 1, 2001. The Company's reserves and future net values are summarized on the following table:

Escalating prices and costs

	Oil & NGL's (Mbbls)		Natural gas (Mmcf)		Present value of future cash flow from Reserves Discounted at			
	Company Gross	Company Net	Company Gross	Company Net	0% M$	10% M$	12% M$	15% M$
Proven developed producing	668.3	550.8	2,879.0	2,121.0	23,219	18,410	17,769	16,922
Proven developed non-producing	115.5	94.4	32.0	23.0	1,073	687	639	577
Proven undeveloped	173.4	133.1	1,565.0	1,181.0	5,384	4,203	4,023	3,778
Total proven	957.2	778.3	4,476.0	3,325.0	29,676	23,300	22,431	21,277
Probable developed	94.7	77.8	221.0	168.0	2,476	1,706	1,607	1,478
Probable undeveloped	314.2	240.8	555.0	414.0	4,961	3,618	3,415	3,140
Total probable	408.9	318.6	776.0	582.0	7,437	5,324	5,022	4,618
Total proven + probable	1,366.1	1,096.9	5,252.0	3,907.0	37,113	28,624	27,453	25,895
Total proven + 50% probable	1,161.7	937.6	4,864.0	3,616.0	33,395	25,962	24,942	23,586

Escalating price forecast

The following table represents an excerpt from price forecasts used by Sproule in their evaluation of Saddle's oil and gas reserves:

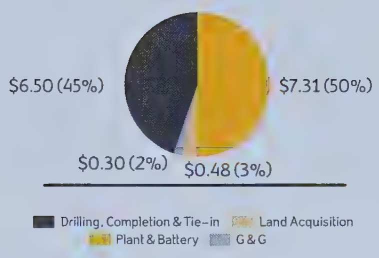
Year	WTI[a] at Cushing Oklahoma ($US/Bbl)	Edmonton[a] par price 40º API ($CDN/Bbl)	Plantgate[b] Alberta Index ($CDN/Mmbtu)
2001	28.20	41.87	7.93
2002	24.41	35.85	5.73
2003	21.12	30.44	4.30
2004	21.44	30.95	3.91
2005	21.76	30.96	3.91
2006	22.08	30.96	3.91

(a) 40º, 0.4% sulphur (b) undeveloped gas must have a minimum $0.15 per MMBtu deduction

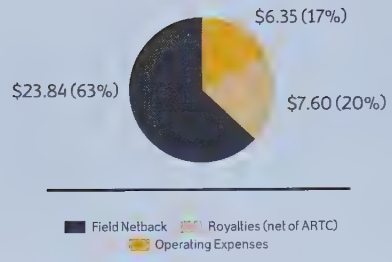
Reserve reconciliation

	Oil and NGLs (Mbbls)			Natural gas (Mmcf)			Oil/NGLs and Gas (Boe's @ 6:1)		
	Proven	Probable[c]	Total	Proven	Probable[c]	Total	Proven	Probable[c]	Total
December 31, 1999	954	298	1,252	1,836	255	2,091	1,260	341	1,601
Discoveries	363	0	363	2,510	0	2,510	782	0	782
Acquisitions	4	0	4	0	0	0	4	0	4
Production	(199)	0	(199)	(850)	0	(850)	(341)	0	(341)
Dispositions	0	0	0	0	0	0	0	0	0
Reserve category change	0	0	0	0	0	0	0	0	0
Revisions to prior estimates	(165)	(93)	(258)	979	133	1,112	(2)	(71)	(73)
January 1, 2001	957	205	1,162	4,476	388	4,864	1,703	270	1,973

(c) Probable reserves have been discounted by a factor of 50% to account for the risk associated with the probability of obtaining production from such reserves



Finding and Development Costs - 2000
($/Boe @ 6:1)



Field Netbacks - 2000
($/Boe @ 6:1)

At January 1, 2001, Saddle's established reserves (proven plus half probable) were comprised of 86% proven reserves. Oil and natural gas liquids formed 59% of total established reserves, while natural gas comprised 41% (70% oil & NGL's and 30% natural gas @ 10:1). The emphasis placed on natural gas exploration in 2000 is evident in the composition of the Company's reserves, as one year earlier Saddle's reserves were comprised 78% oil & NGL's and 22% natural gas (86% oil & NGL's and 14% natural gas @ 10:1).

Saddle's established reserves increased by 23% to 1,973 Mboe in 2000. Established gas reserves increased 133% to 4,864 Mmcf in 2000 from 2,091 Mmcf in 1999. This large increase in gas reserves was due to a 100% success rate in drilling five gas wells in 2000. Saddle anticipates a further increase in gas reserves following the successful drilling of six gas wells in the first quarter of 2001. Established oil and liquids reserves were 1,162 Mbbls in 2000, a decrease of 7% from 1,252 Mbbls in 1999. The decrease in established oil reserves was due to the Company's emphasis on drilling for natural gas in 2000 and to downward reserve revisions of 165 Mboe of proven reserves and 93 Mboe of risked probable reserves mainly due to an oil well that had not performed to expectations. Saddle expects that oil reserves will increase in 2001 as a result of successful drilling of a well into the Keg River LL Pool during the first quarter of 2001.
The reserves associated with this pool could provide a significant increase to the Corporation's oil reserves.

Saddle had proven reserve additions of 784 Mboe, which replaced 230% of 2000 production. The reserve life index for Saddle's established reserves was 5.8 years. Reserve life index is increasing for Saddle as production matures.

Finding and development costs

The following table gives a detailed breakdown of Saddle's capital expenditures for 2000 along with the corresponding contribution to finding, developing and on-stream ("F&D") costs for proven reserves.
The major component of F&D costs was "Plant/Battery and Major Pipelines", representing 50% of the $11.4 million spent by Saddle in the year or $7.31 per Boe. Infrastructure expenditures are, by nature, a painful yet necessary cost component for small companies in their formative stages of growth. Companies much prefer to dedicate available capital directly to drilling and reserve additions. During 2000, in order to solidify its asset base in Rainbow, Saddle made the decision to expend significant capital on infrastructure. In so doing, the Company has been able to gain control of its operations and show a substantial reduction in field operating costs. In the first half of 2000, prior to the infrastructure installation, Saddle had operating costs of $8.72/Boe ($10.09/Boe @ 10:1). Saddle's yearly average for operating costs, which incorporates the first half figures, was $6.35/Boe ($7.61/Boe @10:1). Saddle expects further reductions to operating costs in 2001 as the benefit from the ownership of these facilities is expressed throughout the complete year.

In terms of capital spent directly on proven reserve additions during 2000, Saddle added proven reserves at a cost of $7.28/Boe. Saddle's production stream in Rainbow is comprised of a premium light oil and uncontracted natural gas which combined to generate superior field netbacks of $23.84 /Boe in 2000. This results in a recycle ratio of 3.3 for every dollar invested directly on proven reserve additions during 2000. Overall, including the infrastructure expenditures, Saddle achieved a recycle ratio of 1.6.

Saddle will substantially complete necessary infrastructure additions in 2001. Approximately 25% of the 2001 budget will be spent in this area. Following this investment, the Rainbow property will truly be at the final phase of full cycle development where reserve additions are made at the lowest cost per Boe in the cycle.

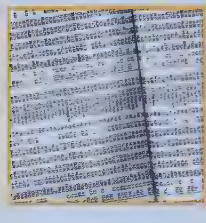
Allocation of Capital Spent in 2000:

	Cost (M$)	Finding and Development (6:1) Proven ($/Boe)
Land acquisition	381	$0.48
G & G	232	$0.30
Drilling	2,401	$3.07
Completion	1,786	$2.28
Plant / battery and major pipelines	5,724	$7.31
Well tie–in costs	897	$1.15
Total Capital Spent (2000)	11,421	$14.59

Drilling

Saddle completed its most active and successful drilling program in Company history in 2000. A total of nine wells were drilled in Rainbow resulting in five gas wells and four oil wells for an overall success rate of 100%. The drilling program targeted three Bluesky gas wells, two Tertiary gas wells and four Keg River oil wells. The following table chronicles Saddle's drilling history over the periods indicated:

	2000		1999		1998		1997	
	Gross	Net	Gross	Net	Gross	Net	Gross	Net
Oil	4.0	2.0	0.0	0.0	5.0	2.3	3.0	0.8
Gas	5.0	2.4	0.0	0.0	0.0	0.0	0.0	0.0
Dry	0.0	0.0	1.0	0.5	0.3	0.8	0.0	0.0
Total	**9.0**	**4.4**	**1.0**	**0.5**	**8.0**	**3.1**	**3.0**	**0.8**
Success rate	100%		0%		63%		100%	
Average working interest	49%		50%		39%		26%	



Management's discussion and analysis

The following discussion is management's review of Saddle's financial and operating results for 2000 and 1999 and should be read in conjunction with Saddle's audited financial statements contained in this annual report.

Fiscal Years Ended December 31, 2000 and December 31, 1999

Changes in accounting policy

In 2000, Saddle adopted the new standard established for the calculation of earnings per share. This standard harmonizes the calculation methodology used under Canadian and United States GAAP. This change is more fully described in Note 2 of the Audited Financial Statements.

Results of operations

In keeping with industry practice, Saddle is moving to a 6:1 ratio for converting natural gas values to a barrel of oil equivalent. Wherever barrels of oil equivalent values are given, the conversion ratio is noted.

Petroleum and natural gas sales – variance analysis

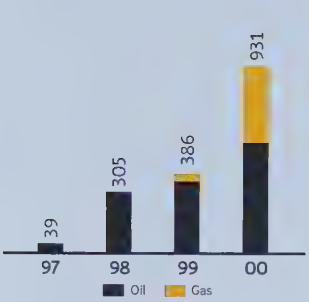
($000's)		Change due to:			
	2000	Pricing	Volume	1999	Change
Total natural gas	$4,720	$2,061	$2,419	$240	1,867%
Crude oil and natural gas liquids					
Sales	8,207	2,460	2,018	3,729	120%
Hedging	(58)	(58)	–	–	–
Total crude oil and natural gas liquids	8,149	2,402	2,018	3,729	119%
Total petroleum and natural gas sales	$12,869	$4,463	$4,437	$3,969	224%

Natural gas sales

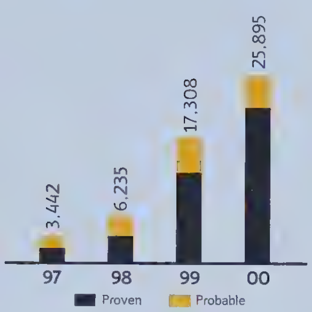
	2000	1999	Change
Natural gas price ($/Mcf)	$5.56	$3.13	78%
Natural gas production (Mcf/d)	2,321	198	1,072%

Crude oil and natural gas liquids sales

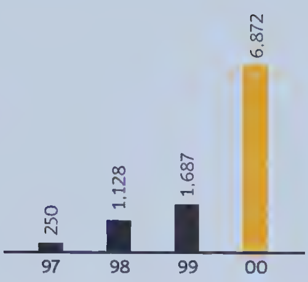
	2000	1999	Change
Crude oil and natural gas liquids price ($/Bbl)	$40.94	$28.87	42%
Crude oil and natural gas liquids production (Bbl/d)	544	353	54%



Average Daily Production, (Boe/d @ 6:1)



Net Present Value (Before Tax)
15 percent DCF, at Dec. 31 ($000)



Cash Flow From Operations, ($000)

Total petroleum and natural gas sales increased 224% to $12.9million for the year ended December 31, 2000 versus $4.0million for 1999. Both natural gas and crude oil and natural gas liquids production increased substantially (1,072% and 54% respectively, as shown in the previous tables). This significant production growth was due to successful drilling. Saddle's natural gas was sold on the spot markets in 2000 at an average price of $5.56/Mcf, a 78% increase from 1999. Saddle produces a very high quality, light crude oil that receives superior wellhead prices. During 2000, the average price received for crude oil and natural gas liquids was $40.94, a 42% increase from 1999.

In 2000, oil hedging losses of approximately $58,000 were netted against related production revenue. This loss arose from a costless collar arrangement, in effect from April 1 to September 30, which fixed both a floor and ceiling price on 300 barrels per day of oil production.

Royalties, net of ARTC:

	2000		1999		Change
	$000's	% Revenue	$000's	% Revenue	
Natural gas	$736	16%	$29	12%	2,438%
Crude oil and natural gas liquids	2,140	26%	985	26%	117%
Alberta royalty tax credit (ARTC)	(286)		(382)		(25%)
Total royalties, net of ARTC	$2,590	20%	$632	16%	310%

Due to higher revenue, royalty expense (net of ARTC) increased 310% to $2.6million for the year ended December 31, 2000 as compared to $0.6million for 1999. Saddle's overall effective royalty rate was 20% compared to 16% in 1999. The increase in the corporate royalty rate was due to an increase in the natural gas royalty rate and a decrease in the total ARTC recovery. Natural gas royalty rates are price sensitive, thus rates increase as gas prices increase. Even though crown royalties eligible for ARTC increased in 2000, the total ARTC recovery decreased because only 26% of eligible crown royalties could be recovered as compared to 69% in 1999.

Processing income

Saddle recorded approximately $78,000 for processing income for the year ended December 31, 2000.
The Company did not have any processing income in 1999. During 2000, Saddle constructed a major oil facility, installed gas compression and pipeline infrastructure as well as purchased an operated interest in a second oil facility. Saddle transferred the majority of its oil production from third party facilities to its own facility as well as tied-in its new gas production to its new gas facility. In addition to its own production, Saddle also processed some third party production through its facilities and this generated processing income.

Operating expenses

	2000		1999		Change
	$000's	$/Boe @ 6:1 (10:1)	$000's	$/Boe @ 6:1 (10:1)	
Operating expenses	$2,242	$6.58 ($7.90)	$1,133	$8.04 ($8.32)	98%
Processing income	(78)	$0.23 ($0.29)	–	–	–
Operating expenses, net of processing income	$2,164	$6.35 ($7.61)	$1,133	$8.04 ($8.32)	91%

Operating costs on a per unit of production basis were reduced to $6.35/Boe ($7.61/Boe 10:1) as compared to $8.04/Boe ($8.32/Boe 10:1) in 1999. Total operating expenses, net of processing income, increased 91% to $2.2million for the year ended December 31, 2000 due to higher production volumes. At year end 2000, approximately 90% of Saddle's production was processed through Company owned and operated facilities. Saddle was therefore better able to control its operations and reduce third party processing charges, which resulted in reduced operating costs.

Field netback

	2000		1999		Change
	$000's	$/Boe @ 6:1	$000's	$/Boe @ 6:1	
Petroleum and natural gas sales	$12,869	$37.78	$3,969	$28.17	224%
Royalties, net of ARTC	(2,590)	(7.60)	(632)	(4.49)	310%
Processing income	78	0.24	–	–	–
Operating expenses	(2,242)	(6.58)	(1,133)	(8.04)	98%
Field netback	$8,115	$23.84	$2,204	$15.64	268%

Saddle's field netback for the year ended December 31, 2000 was $8.1million, a 268% increase from 1999. This was due to increased production volumes and prices. Netback on a per unit of production basis improved to $23.84/Boe, a 52% increase from $15.64/Boe in 1999. Positive factors such as higher product prices, higher processing income and lower operating expenses were only partially offset by higher royalties.

General and administrative expenses

	2000			1999			Change
	$000's	%	$/Boe @ 6:1	$000's	%	$/Boe @ 6:1	
Expensed	$1,267		$3.72	$660		$4.68	92%
Recoveries	(452)		(1.33)	(163)		(1.16)	177%
Admin fee income	–		–	(58)		(0.40)	–
Net expensed	815	81%	2.39	439	70%	3.12	86%
Capitalized	190	19%	0.56	183	30%	1.29	4%
Total	$1,005	100%	$2.95	$622	100%	$4.41	62%

General and administrative expenses per unit were reduced to $2.39/Boe 2000 due to the economies of scale associated with managing a larger production and reserve base. Total general and administrative expenditures increased 62% to $1.0million in 2000 primarily due to increased salaries, wages and consulting fees reflective of the growth in the Company's operations. Recoveries increased 177% to $452,000 due to Saddle acting as operator for the majority of its 2000 capital projects and related production.

Interest expense

For the year ended December 31, 2000, Saddle had interest expense of $410,000 compared to $74,000 for 1999. Interest on bank debt accounted for $390,000 while interest relating to a capital lease obligation totaled $20,000. During the year, Saddle implemented a large capital program that was financed through cash flow from operations and the Company's credit facility. The capital expenditure program exceeded cash flow from operations and this resulted in bank debt of $6.9million at December 31, 2000. Through the use of bankers' acceptances, the Company achieved an effective interest rate on bank debt of 5.66% as at December 31, 2000.

Depletion and depreciation

	2000		1999		Change
	$000's	$/Boe @ 6:1	$000's	$/Boe @ 6:1	
Oil and gas	$3,837	$11.27	$1,141	$8.10	236%
Office furniture and equipment	28	0.08	33	0.23	(15%)
Site restoration	226	0.66	79	0.57	186%
Total Provision	$4,091	$12.01	$1,253	$8.90	226%

The depletion, depreciation and restoration provision for the year ended December 31, 2000 was $4.1million, an increase of 226% from 1999. This increase was due to both production volume growth and an increased depletion rate for oil and gas assets. The 2000 depletion and depreciation rate increased primarily due to capital expenditures on infrastructure such as the construction of a major oil facility, gas compression and a pipeline; costs that are not directly attributable to finding reserves but are integral to realizing the benefits of full cycle exploration.

Future income taxes

Future income taxes for the year ended December 31, 2000 were $637,000 resulting in an effective tax rate of 23%. There were no future income taxes on the income statement for 1999, as Saddle had an unrecognized tax asset arising from its tax pools exceeding the net book value of capital assets. The increase in the 2000 future income tax provision over 1999 is the result of both higher earnings before taxes. The following table is an approximate breakdown of tax pools at December 31, 2000.

$000's	
COGPE	$6,142
CDE	2,854
CCA pools	7,976
Non-capital losses	440
Share issue costs	673
Total	$18,085

Liquidity and capital resources

Capital expenditures

Capital expenditures were $11.4 million for the year ended December 31, 2000. The 2000 capital expenditure figure is comprised of land expenditures of $0.4 million, geological and geophysical expenditures of $0.2 million, drilling, completion and well tie-in costs of $5.1 million and plant, battery and compressor costs of $5.7 million. During 1999, capital expenditures totaled $10.0 million, $6.4 million of which related to the acquisition of the Rainbow property.

Cash flow

Funds to support ongoing corporate initiatives were obtained from two primary sources: internally generated cash flow from operations and bank lending. For the year ended December 31, 2000 Saddle utilized $6.9million of cash flow and $4.5million of bank debt to finance the capital program.

Cash flow from operations in 2000 totaled $6.9million, a 307% increase from 1999. Cash flow per share was $0.44 ($0.44 diluted) in 2000 versus $0.21 ($0.16 diluted) in 1999. The growth in cash flow in 2000 is due to increased production and higher field netbacks.

The following table shows cash flow and discretionary cash flow per unit (Boe @ 6:1):

	2000		1999	
	$000's	$/Boe @ 6:1	$000's	$/Boe @ 6:1
Field netback	$8,115	$23.84	$2,204	$15.64
General and administrative expenses	(815)	(2.39)	(439)	(3.12)
Interest expense	(410)	(1.21)	(74)	(0.52)
Capital taxes	(18)	(0.06)	(4)	(0.03)
Cash flow from operations	6,872	20.18	1,687	11.97
Capitalized general & administrative	(190)	(0.56)	(183)	(1.29)
Discretionary cash flow	$6,682	$19.62	$1,504	$10.68

Long term debt – bank loan

Saddle had a financing arrangement with a Canadian chartered bank for a $7.5 million extendible revolving term production loan with interest payable monthly at the bank prime rate. As at December 31, 2000 Saddle had drawn $6.9 million on the credit facility (1999 - $2.4million). The facility is secured by a $35 million floating charge debenture over all of the assets of the Company and a general assignment of book debts. The bank has confirmed that no principal repayments of the facility will be required before January 1, 2002, provided that the Company continues to satisfy the provisions of the credit agreement and maintains an adequate borrowing base. Accordingly, the debt was classified as long-term in the financial statements.

Long term debt – capital lease

During 2000, Saddle entered into a lease that is being treated as a capital lease for accounting purposes. Please refer to the Audited Financial Statements, Note 5 for further discussion about this lease.

Equity

Pursuant to an offering memorandum dated September 15, 1999, Saddle issued special warrants, with each special warrant being convertible into one common share at no additional cost. On January 21, 2000 a prospectus qualified for distribution of the shares issuable upon exercise of the warrants and the warrants were exercised.

Saddle's net asset value per share at December 31, 2000 was $1.16 per share, an increase of 33%, as illustrated in the table below.

Net asset value

	2000 $000's	1999 $000's	Change
Reserves (discounted @ 15% before income taxes)			
Proven	$21,277	$12,070	76%
50% Probable	2,309	2,619	(12%)
	$23,586	$14,689	61%
Undeveloped Land	1,958	1,696	15%
Working Capital	(239)	(413)	–
Long Term Debt	(7,153)	(2,404)	–
Net Asset Value	$18,152	$13,568	34%
Common shares / warrants outstanding	15.6 million	15.6 million	–
Net asset value per share	$1.16	$0.87	33%

Business risks

Crude oil and natural gas operations involve certain risks and uncertainties. These risks include, but are not limited to, future commodity prices, exchange rates, interest rates, geological risk, reservoir risk, political risk and product demand and transportation restrictions.

The Company is continually reviewing means to mitigate these risks by utilizing a combination of internal controls, sound operating practices, insurance and hedging. Saddle focuses activities in areas where it believes it has sufficient technical expertise to be successful while maintaining an inventory of prospects. The Company has pursued exploration and development in its core area of Rainbow Lake in northern Alberta, where it has a good understanding of the geological risks and potential. The Company maintains insurance coverage to protect against pollution, well blowouts and other types of unanticipated occurrences that may affect the Company's assets. Risks associated with commodity prices, interest and exchange rates are generally beyond the control of the Company; however, Saddle may consider various hedging products to reduce the volatility in these areas. Environmental and safety risks are addressed by compliance with government regulations as well as adoption and compliance of the Company's safety and environmental standards policy.

Management's report

The annual report and financial statements have been prepared by management who, where necessary, have made informed judgments and estimates of the outcome of events and transactions, with due consideration given to materiality. Management acknowledges responsibility for the fairness, integrity and objectivity of all information contained in the annual report, including the financial statements.

As a means of fulfilling its responsibility, management relies on the Company's system of internal control. This system has been established to ensure, within reasonable limits, that assets are safeguarded, transactions are properly recorded and executed in accordance with management's authorization and that accounting records provide a solid foundation from which to prepare the financial statements.

The Board of Directors carries out its responsibility for the financial statements principally through its Audit Committee, the majority of which are non-management directors. This committee meets periodically, reviews the scope of the external audit, the adequacy of the system of internal control and the appropriateness of the financial reporting and then makes its recommendations to the Board. Based on those recommendations, the Board of Directors approves the financial statements.

William S. Ward
President and Chief Executive Officer

May 1, 2001

Auditors' report to shareholders

We have audited the balance sheets of Saddle Resources Inc. as at December 31, 2000 and 1999 and the statements of operations and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2000 and 1999 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

KPMG LLP

KPMG LLP
Chartered Accountants

Calgary, Canada
March 12, 2001

Balance sheets

As at December 31, 2000 and 1999	2000	1999
Assets		
Current assets:		
Cash and term deposits	$ –	$ 491,513
Accounts receivable	4,025,839	4,123,974
Prepaid expenses and deposits	186,421	180,501
	4,212,260	4,795,988
Capital assets (note 3)	19,898,318	12,341,197
	$ 24,110,578	$ 17,137,185
Liabilities and shareholders' equity		
Current liabilities:		
Accounts payable and accrued liabilities	$ 4,403,662	$ 5,208,494
Current portion of capital lease (note 5)	47,554	–
	4,451,216	5,208,494
Bank loan (note 4)	6,888,367	2,403,921
Capital lease (note 5)	264,766	–
Provision for future site restoration (note 3)	337,657	111,523
Future income taxes (note 7)	637,028	–
Shareholders' equity:		
Share capital (note 6)		
Common Shares	12,053,358	5,916,258
Special warrants	–	6,163,343
	12,053,358	12,079,601
Deficit	(521,814)	(2,666,354)
	11,531,544	9,413,247
	$ 24,110,578	$ 17,137,185

Commitments (note9). See accompanying notes to financial statements.

Approved by the Board:

William S. Ward
Director

Kenneth L. Broadhurst
Director

Statements of operations and deficit

Years ended December 31, 2000 and 1999	2000	1999
Revenue:		
Petroleum and natural gas sales	$ 12,868,565	$ 3,969,074
Royalties, net of ARTC	(2,589,563)	(631,803)
Processing income	78,480	–
	10,357,482	3,337,271
Expenses:		
Operating	2,242,421	1,132,808
General and administrative	815,006	439,355
Interest	410,279	73,503
Depletion and depreciation	4,090,633	1,253,282
Capital taxes	17,575	4,831
	7,575,914	2,903,779
Earnings before income taxes	2,781,568	433,492
Future income taxes (note 7)	637,028	–
Net earnings	2,144,540	433,492
Deficit, beginning of year	(2,666,354)	(3,099,846)
Deficit, end of year	$ (521,814)	$ (2,666,354)

See accompanying notes to financial statements

	2000	1999
Earnings per share (note 6) – basic	$ 0.14	$ 0.05
Earnings per share (note 6) – diluted	$ 0.14	$ 0.04

Statements of cash flows

Years ended December 31, 2000 and 1999	2000	1999
Cash provided by (used in):		
Operations:		
Net earnings	$ 2,144,540	$ 433,492
Add non-cash items		
Depletion and depreciation	4,090,633	1,253,282
Future income taxes	637,028	–
Cash flow from operations	6,872,201	1,686,774
Net change in non-cash working capital (note 11)	62,561	(1,083,100)
	6,934,762	603,674
Investing:		
Additions to capital assets	(11,421,620)	(10,017,170)
Net change in non-cash working capital (note 11)	(775,178)	442,462
	(12,196,798)	(9,574,708)
Financing:		
Issuance of common shares and warrants for cash, net of issue costs of $621,657	–	6,569,050
Share issue costs incurred upon exercise of warrants	(55,043)	–
Repayment of shareholder loans	28,800	–
Increase in bank loan	4,484,446	1,353,921
Increase in capital lease	312,320	–
	4,770,523	7,922,971
Decrease in cash	(491,513)	(1,048,063)
Cash and term deposits, beginning of year	491,513	1,539,576
Cash and term deposits, end of year	$ –	$ 491,513

See accompanying notes to financial statements.

Notes to the financial statements

For the years ended December 31, 2000 and 1999

1. Basis of presentation:

Saddle Resources Inc. (the "Company") was incorporated under the laws of the province of Alberta on January 4, 1996. On October 20, 1998 Netalco Corporation ("Netalco") acquired all of the issued and outstanding shares of the Company, a private company in the business of exploration, development and production of petroleum and natural gas properties. These financial statements have accounted for the business combination as a reverse takeover and the Company is considered to have acquired Netalco. Accordingly, these financial statements reflect the results of operations of the Company from inception.

On January 13, 1999, the Company consolidated its common shares on a 5 for 1 basis. All share and per share amounts in the financial statements reflect the consolidated share structure.

2. Significant accounting policies:

(a) Capital assets:

The Company follows the full cost method of accounting for its petroleum and natural gas operations, whereby all costs relating to the acquisition, exploration and development of petroleum and natural gas reserves are capitalized into cost centres. Such costs include land acquisition costs, geological and geophysical costs, lease rental costs on non-producing properties, costs of drilling both productive and non-productive wells and overhead charges directly related to acquisition, exploration and development activities.

Capitalized costs together with production and related equipment, excluding costs relating to unproven properties, are depleted and depreciated using the unit-of-production method based on estimated proven petroleum and natural gas reserves before royalties as determined by independent petroleum engineers. For purposes of the depletion calculation, gross proven natural gas reserves and production are converted to equivalent volumes of petroleum based on the approximate relative energy content.

The Company applies a "ceiling test" to capitalized costs to ensure that such costs do not exceed future net revenues from estimated production of proven reserves, using prices and costs in effect at year-end, and the costs of unproven properties less impairment. Future net revenues are undiscounted and are calculated after deducting general and administrative costs, financing costs, income taxes and site restoration costs. Capitalized costs in excess of this ultimate recoverable amount are charged to earnings.

Proceeds on the disposition of petroleum and natural gas properties are applied against capitalized costs, with gains or losses not ordinarily recognized, unless such a sale would result in a greater than 20% change in the depletion and depreciation rate.

Depreciation of furniture and office equipment is provided using the declining balance method at rates varying between 20% and 30%.

(b) Interest in joint ventures:

Some of the Company's petroleum and natural gas exploration, development and production activities are conducted jointly with others and, accordingly, the financial statements reflect only the Company's proportionate interest in such activities.

(c) Future site restoration costs:

Site restoration costs are provided for over the life of the estimated proven reserves on a unit-of-production basis. Costs are estimated each year by management in consultation with the Company's engineers based on current regulations, costs, technology and industry standards. The period charge is included in depletion and depreciation expense and actual site restoration expenditures are charged to the accumulated provision account as incurred.

(d) Use of estimates:

Management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements as well as reported amounts of revenues and expenses during the reported period. Actual results could differ from these estimates.

(e) Revenue recognition:

Revenues associated with the sales of natural gas, natural gas liquids and crude oil owned by the Company are recognized when title passes from the Company to its customer.

(f) Financial instruments:

The Company uses derivative financial instruments from time to time to hedge its exposure to commodity price and foreign exchange fluctuations. All transactions are related to an underlying physical position or to future oil and natural gas production and this hedging relationship is or is expected to be effective. The Company does not use derivative financial instruments for trading purposes.

Gains and losses on financial instruments designated as hedges are deferred and are recognized in the period and in the same financial category in which the revenues or expenses associated with the hedged transactions are recognized.

(g) Income taxes:

The Company records income taxes using the liability method of tax allocation accounting. Under the liability method, the Company records future income taxes for the effect of any difference between the accounting and income tax basis of an asset or liability. Future income tax assets or liabilities are adjusted to reflect substantively enacted income tax rates.

An estimate of the future income tax liability to be incurred on flow-through share arrangements is recognized and charged to share capital.

(h) Per share amounts (see Note 6(f)):

Basic earnings per share and cash flow from operations per share are computed by dividing the earnings and cash flow from operations by the weighted average number of shares outstanding during the period.

Diluted per share amounts are calculated giving effect to the potential dilution that would occur if options to purchase common shares were exercised. The Company has adopted the treasury stock method, in accordance with recommendations of the Canadian Institute of Chartered Accountants, to determine the dilutive effect of stock options. The new policy has been adopted retroactively and no restatement of prior period amounts was required as a result of adoption of the new accounting policy. The treasury stock method assumes that proceeds received from the exercise of in-the-money stock options are used to repurchase common shares at the prevailing market rate.

(i) Cash and term deposits:

Cash and term deposits consist of cash in the bank, less outstanding cheques and short-term deposits with a maturity of less than three months.

(j) Stock based compensation plan:

Consideration paid by directors, employees and consultants on the exercise of stock options under the stock option plan is recorded as share capital. No compensation expense is recognized with respect to stock options as the exercise price equals the market price of shares on the date of the grant.

3. Capital assets:

	2000	1999
Petroleum and natural gas interests	$ 29,942,717	$ 18,872,413
Equipment under capital lease	347,855	–
Other	167,365	163,904
	30,457,937	19,036,317
Accumulated depletion and depreciation	(10,559,619)	(6,695,120)
	$ 19,898,318	$ 12,341,197

During the year ended December 31, 2000, the Company capitalized $190,000 (1999 – $183,000) of general and administrative costs related to exploration and development activity.

At December 31, 2000, the depletion calculation excluded unproven properties of $1,464,000 (1999 – $1,696,000). Future development costs of proven undeveloped reserves of $2,725,000 (1999 – $1,167,000) are included in the depletion and depreciation calculations.

At December 31, 2000 the estimated future site restoration costs to be accrued over the remaining proved reserves are $1,011,000 (December 31, 1999 – $1,035,000).

4. Bank loan:

At December 31, 2000, the Company had a financing arrangement with a Canadian chartered bank for a $7,500,000 extendible revolving term production loan with interest payable monthly at the bank prime rate. The facility is secured by a $35,000,000 floating charge debenture over all of the assets of the Company and a general assignment of book debts. At December 31, 2000, the Company had outstanding advances on the revolving loan of $6,888,367 (December 31, 1999 – $2,403,921). The bank has confirmed that no principal repayments of the facility will be required before January 1, 2002, provided that the Company continues to satisfy the provisions of the credit agreement and maintains an adequate borrowing base. Accordingly, the debt was classified as long-term in the financial statements.

5. Capital lease:

During 2000, the Company entered into a lease for a field compressor that is being treated as a capital lease for accounting purposes. The equipment is furnished as security for the capital lease and the lease is repayable in monthly installments of $6,500, bearing interest at 10.4% per annum. The Company is required to make the following annual principal repayments:

	2000
2001	$ 47,554
2002	52,758
2003	58,532
2004	64,937
Thereafter	88,539
Less current portion	(47,554)
Capital lease	$ 264,766

Interest of $19,900 (1999 – nil) relating to the capital lease obligation has been included in interest expense.

6. Share capital:

(a) Authorized:

Unlimited number of common shares, without nominal or par value; and
Unlimited number of preferred shares, without nominal or par value.

(b) Common shares issued:

	Number of Shares	Amount
Common shares:		
Balance December 31, 1998	7,735,720	$ 5,510,551
Private placement	900,000	405,000
Options exercised	1,504	707
Balance December 31, 1999	8,637,224	$ 5,916,258
Shares issued upon exercise of warrants, net of share issue costs of $55,043	7,000,000	6,108,300
Shareholder loan partial repayment (1)		28,800
Balance December 31, 2000	15,637,224	$12,053,358

(1) In 1998, the Company advanced $57,500 to two officers and directors to acquire shares in the Company. The notes bear interest at 5% per annum, payable at the end of each year, with the principal payable on or before December 31, 2003. During 2000, $28,800 of this loan was repaid.

(c) Special warrants:

	Number of Special warrants	Amount
Balance December 31, 1998	–	$ –
Flow-through special warrants	1,350,000	1,417,500
Special warrants	5,650,000	5,367,500
Warrant issue costs		(621,657)
Balance December 31, 1999	7,000,000	$ 6,163,343
Special warrants exercised to shares	(7,000,000)	(6,163,343)
Balance December 31, 2000	–	$ –

Pursuant to an offering memorandum dated September 15, 1999, the Company issued 5,650,000 special warrants and 1,350,000 flow-through special warrants at $0.95 and $1.05 each, respectively. Each special warrant is convertible into one common share at no additional cost. On January 21, 2000 a prospectus qualified for distribution of the shares issuable upon exercise of these warrants.

d) Flow-through shares:

In accordance with the terms of the Company's various flow-through share offerings, and pursuant to certain provisions of the Income Tax Act, the Company was committed to renounce, for income tax purposes, exploration and development expenditures to the purchasers of its flow-through shares in the aggregate amount of $1,417,500 in 1999. At December 31, 1999 $931,334 of renounced flow through expenditures were remaining to be incurred in 2000. These expenditures were incurred during 2000.

e) Stock options:

The directors of the Company have approved stock options whereby common shares of the Company will be available for purchase by directors, officers, employees, and other persons providing services to the Company. At December 31, 2000 a total of 1,115,000 (1999 – 638,496) options were authorized and have been granted to purchase 1,115,000 (December 31, 1999 – 638,496) common shares of the Company at prices ranging from $0.45 to $1.20 per share at various dates to December 11, 2005. These options have a weighted average remaining contractual life of 3.7 years.

	2000 Number of options	2000 Weighted avg. exercise price	1999 Number of options	1999 Weighted avg. exercise price
Stock options outstanding, beginning of year	638,496	$0.83	497,333	$1.35
Granted	526,504	$0.65	240,000	$0.58
Exercised	–	–	(1,504)	$0.47
Cancelled or expired	(50,000)	$0.78	(97,333)	$2.83
Stock options out standing, end of year	1,115,000	$0.75	638,496	$0.83
Exercisable at year end	267,860	$0.87	117,860	$0.91

f) Net earnings and cash flows from operations per share:

	2000	1999
Net earnings per share – basic	$ 0.14	$ 0.05
Net earnings per share – diluted	$ 0.14	$ 0.04
Cash flow from operations – basic	$ 0.44	$ 0.21
Cash flow from operations – diluted	$ 0.44	$ 0.16
Weighted average number of shares outstanding (000's) – basic	15,637	8,187
Weighted average number of shares outstanding (000's) – diluted	15,784	10,327

7. Income taxes:

The following table reconciles income taxes calculated at the Canadian statutory rate of 44.6% (1999 – 44.6%) with actual income taxes:

	2000	1999
Tax expense @ 44.6% of earnings before tax	$ 1,248,418	$ 193,337
Crown payments not deductible for tax purposes	1,282,796	405,045
Resource allowance	(933,019)	(234,189)
Alberta Royalty Tax Credit	(127,768)	(170,358)
Renounced on flow-through shares	415,375	–
Share issue costs	(24,549)	–
Valuation allowance	(1,229,665)	(197,608)
Other	5,440	3,773
	$ 637,028	$ –

The components of the net future income tax asset (liability) at December 31, 2000 and 1999:

	2000	1999
Future income tax assets:		
Tax basis of capital assets in excess of carrying value	$ –	$ 242,632
Non-capital loss carry-forwards	–	589,774
Share issue costs	300,130	350,614
Future removal and site restoration costs	112,946	37,304
Other	9,341	9,341
Valuation allowance	–	(1,229,665)
	422,417	–
Future income tax liabilities:		
Carrying value of capital assets in excess of tax basis	(1,059,445)	–
Net future income tax liability	$ (637,028)	$ –

8. Related party transactions:

(i) In June 1999, the Company and a joint interest partner who held 21% of the Company's common shares acquired certain oil and gas properties for $12 million. The Company initially acquired a 5 % interest in these properties and then, on October 7, 1999, exercised an option to acquire an additional 45% interest from its joint interest partner for an amount equal to 45% of the acquisition cost of the properties of $12 million plus accrued interest.

(ii) As at December 31, 2000 the joint interest partner holds approximately 12.5% of the Company's total issued and outstanding common shares.

The joint interest partner participates with the Company in certain oil and natural gas joint ventures on the same terms and conditions as other industry partners. As at December 31, 2000, the Company had a current receivable in the amount of $932,645 (1999 – $2,431,846) from the joint interest partner, which was received subsequent to year-end.

9. Commitments:

At December 31, 2000, the Company has committed to future minimum payments under various operating leases that cover office facilities and a vehicle for each of the next five years of approximately: 2001 – $131,000; 2002 – $129,000; 2003 – $121,000 and 2004 – $40,000.

10. Financial instruments:

Effective April 1,2000 and terminating on September 30,2000, the Company had a costless collar arrangement which fixed both a floor and ceiling price on 300 barrels per day of oil production. Throughout the term of this arrangement a total loss of $58,740 was recognized and recorded against Petroleum and Natural gas sales.

The fair values of financial assets and liabilities that are included in the balance sheet approximate their carrying amounts due to the short-term maturity of those instruments.

Substantially all of the Company's accounts receivable are with customers in the oil and gas industry and are subject to normal industry credit risks.

11. Supplemental cash flow disclosure:

The following cash payments have been made during the year:

	2000	1999
Interest paid	$ 410,279	$ 73,503
Taxes paid	$ 4,340	$ –

Changes in non–cash working capital balances:

	2000	1999
Operations:		
Accounts receivable	$ (919,902)	$ (1,174,906)
Prepaid expenses and deposits	(5,920)	(121,665)
Accounts payable and accrued liabilities	988,383	213,471
	$ 62,561	$(1,083,100)
Investing:		
Accounts receivable	$ 1,018,037	$(2,012,636)
Accounts payable and accrued liabilities	(1,793,215)	2,455,098
	$ (775,178)	$ 442,462

12. Comparative figures:

Certain prior year figures have been restated to conform with current year presentation.

Corporate information

Management
William S. Ward
President & CEO

Kenneth L. Broadhurst
Senior Vice President

Kevin D. Bibault
Vice President of Engineering

Kelly Tomyn
Controller

Directors
J. Cameron Bailey

Colin D. Boyer

Troy K. Brazzoni

Matthew J. Brister

Kenneth L. Broadhurst

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Registrar & Transfer Agent
Valiant Corporate Trust Company
Calgary, Alberta

Abbreviations

$CDN	Canadian dollar
$US	United States dollar
API	American Petroleum Institute
ARTC	Alberta Royalty Tax Credit
Bcf	Billions of cubic feet
Boe	Barrels of oil equivalent (6 Mcf of natural gas being equivalent to one barrel of oil, unless otherwise noted)
Boe/d	Barrels of oil equivalent per day
Bopd	Barrels of oil per day
Bbls	Barrels of oil or natural gas liquids
Bbls/d	Barrels per day
Mbbls	Thousands of barrels
Mboe	Thousands of barrels of oil equivalent
Mcf	Thousands of cubic feet
Mcf/d	Thousands of cubic feet per day
Mmbtu	Millions of British thermal units
Mmcf	Millions of cubic feet
Mmcf/d	Millions of cubic feet per day
Mstb	Thousand stock tank barrels
NGL	Natural Gas Liquids
NPV	Net Present Value
WTI	West Texas Intermediate

Back row: Greg Parry, Kevin Bibault, Mike Huculak, Ken Broadhurst, Bill Ward, Terry Kraychy
Front row: Lindsay Kilgour, Laura Hatch, Doug Smith, Karen Bolduc and Kelly Tomyn Missing: Linda Pullar and Mike Roth

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